

**March 28, 2008 Committee Meeting of the
Nonprofit and Unincorporated Organizations Committee
of the Business Law Section of the State Bar of California**

Minutes of Program
Conversation with Susan Willett, CPA,
Technical Specialist, Program Specialist II,
and Dave Isaac, Program Specialist I,
Franchise Tax Board

A. Susan Willett reported that the FTB had met the previous day and had made the following decisions:

1. Legal Notice – AB 897 has caused a lot of confusion. It does not require the FTB to send a determination letter or acknowledgment of any kind. A separate acknowledgement was developed because the determination letter includes Taxpayer Bill of Rights provisions under R&TC 21012. The lack of a determination letter has caused some issues with others. The FTB will issue a legal notice explaining that because of AB 897, the only document the charities will receive from the FTB is an acknowledgement postcard [note -- since meeting, acknowledgement letter], which will be in place of a determination letter. Normally, a legal notice takes some time, but because this is a sensitive issue, it will be issued quickly, hopefully in 30 days.

2. Group Exemptions – under federal law, an organization may be incorporated as a chapter and come under the parent's group exemption. The FTB will change the regulation in California to correspond with federal law so that both incorporated and unincorporated organizations may come under the group exemption. As of January 1, 2008, the FTB will allow incorporated subordinates to qualify under the group exemption of the parent if the parent submits the 3500A with their federal determination letter and a list of all the chapters that they wish to include in the group exemption. If some of the chapters are incorporated the FTB will still add them to the exemption.

B. Postcard Acknowledgment [note below, Postcard will be replaced by a letter] – as mentioned above, under AB 897, the FTB is not required to send any response upon the submission of a federal determination letter. As a courtesy, to let an organization know that its submission was received, the FTB is sending an acknowledgement postcard [letter]. In the past, other agencies have relied upon the California determination letter. The FTB legal notice will inform the public of the amendment to the law and follow up acknowledgement postcard [letter]. Other agencies may need to have their laws amended, such as county ordinances that use specific language referencing a California determination letter. The postcard [letter] is not a legal document; it is just a courtesy notice so that who ever needs it will have something that confirms the exempt status of the organization under California law. If an organization finds it needs to have a California determination letter, it would still have to apply for exemption under California law. The text of the postcard is: "This letter acknowledges that the FTB received your determination that shows that it is exempt under 501(c)(3). Any change to the operation or exemption will require that"

[It was subsequently decided that the Postcard Acknowledgement would not be used. Instead, an acknowledgement letter will be sent to the organization showing it is

exempt. Legal has a draft that is currently being reviewed to replace the Postcard Acknowledgement.]

C. Proposed Changes to the Chaptered Law (AB 897) – AB 897 – the bill started out originally to modify 23701. The federal exemption is all inside 501. In California, each code section is a stand alone law. We have 24 different types of exemptions, and any of our California exemptions can be a group, which is why the group exemption was in the regulations of 23701.

D. Conformity with Federal Law – Susan said the FTB understands that having conformity with federal law probably is a good idea. There are other areas also that should be brought into conformity. For example:

1. Under federal law there is an advance ruling period. Susan Willett said we have a hard time working with the IRS because it relies on the 5 year advance ruling period to determine whether or not the charity will actually qualify.

2. Federal law has interim sanctions. The FTB only has loss of exemption or revocation, so the FTB must look at the application much more narrowly. The IRS knows it can do an excise tax to teach the charity to do better, but the FTB does not have that option, so the FTB wants to be sure the charity will be okay from the start.

3. c4s, c5s, c6s and c7s.

Question – There are other organizations besides c3s and 23701ds that are essentially the same under federal and state law. Under federal law, for anything but a c3 you do not need to apply for exemption, but many apply nevertheless. Would it make sense to have the AB 897 law also apply to those organizations if they establish their exempt status with the IRS?

Answer – That is a very good question. Churches have to apply for California exemption, and they do not have to under federal law. The feds actually like that. I think you are referring to the social clubs under federal law; we match pretty well.

Yes – also to c4's, 5's and 6's.

E. Consensus on Desire to Clean up AB 897 and on Conformity with Federal Law

1. Committee Chair Lisa Runquist said let's try to clean up AB 897 so the FTB is happy with it and we are happy with it, too; it makes sense to look at the whole issue, as well.

2. Louis, Chair of the Exempt Organizations Committee, said his Committee is on board with this desire as well; however, full conformity probably would have to be a separate bill. The EO Committee of the Tax Section is very interested in working with the Nonprofit Organizations Committee of the BLS. Susan Willett and Dave Isaac will speak to that committee on the same topic at that committee's April 11 telephone conference call meeting. Anyone from the Nonprofit Committee is welcome to join. Susan said she has thought a long time about private foundations and the interim sanctions. She will try to get another attorney to try to attend on the April 11 call. [Note, since the meeting, no one from FTB will be able to attend the EO Committee meeting April 11.]

3. It was decided that in order to help the two committees work together and move the discussion forward, minutes of this meeting would be circulated to both committees before the April 11 meeting to eliminate going over the same ground in the EO Committee meeting.

4. Drafting Committee – If we had both the BLS and the Tax section and the FTB in agreement on the language, the State Bar is likely to approve and locate someone to introduce the bill. Are there people that would like to serve on the drafting committee? Lani, Louis, Gary, Lisa, Cherie and Patrick volunteered.

5. Other problems with AB 897 – Even though AB 897 allows the FTB to do a revocation, if the organization submits the federal determination letter, then it would be exempt again under AB 897, and we would have to revoke again, a circular problem. The proposed change to the chaptered law would provide that the organization would not be able to reinstate the exemption until evaluated.

F. Susan Willett Replacement – Susan is transferring out of exempt. Dave Isaac will be her replacement. Dave provided some of his background. He has spent 8 years in disclosure.

G. Staffing Levels – Timing of Response – The FTB is running behind. Normally it is 90 days, but right now it is taking closer to 4 months before an application for exemption is being assigned. There is a back log now.

Q – From receipt of application to issuing a “need more info letter” or the determination – Are you at 6 months?

A – No, we are still at 4 months, working over time. By summer we will be down to a drawer or two. In the winter months, we usually get more applications.

Due to FTB sending out filing enforcements on a continuous basis the amount of applications received is not expected to decrease as in previous years.

[Additional Notes: The form 3500A has been pulled from the FTB web site. Legal is having the form revised to remove all the questions. The form will be simplified and less intrusive. The form should be available on FTB web site within 3 weeks.]

Respectfully Submitted,
Lani Meanley Collins, Vice-Chair, Web site